STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 98-924

June 2, 1999

PORTLAND WATER DISTRICT
PROPOSED RATE CHANGE
(DECREASE OF 8%)

Order (Part II)

I. SUMMARY

In this Order, we establish filing requirements for a second phase in this case. The purpose of this second phase is to determine whether the Portland Water District's proposed rate design of a 15% differential between nonmember communities and member communities is just and reasonable. We allow the Portland Water District (District) to implement its proposed rate design, on an interim basis, based on the parties' agreement or lack of objection to an interim implementation of the differential during the pendency of the Phase II proceeding. In addition, we decide to allow the differential as it relates to the Town of Yarmouth because Yarmouth did not object to the differential and because the rate for water supplied to the District for resale by Yarmouth is negotiated between Yarmouth and the District. Finally, we decline the Public Advocate's invitation to consider in this case the issue of whether the Commission should change its practice of allowing consumer-owned water utilities to recover in rates depreciation on plant and the annual principal payments on the debt used to purchase that plant. Our Part I Order, issued on April 30,1999, outlined these findings. In this Part II Order, we describe the bases for our decision and set forth information filing requirements for Phase II.

Because the amount of revenue involved in this matter is quite small[1] and the cost of litigating the question of the differential may be significant, the District should consider whether pursuing this matter is a wise use of ratepayer funds. Thus, we request that the District notify us by June 15, 1999 to indicate whether it intends to proceed to Phase II. If the District does not proceed to Phase II, we will reserve the issue of the member/nonmember distinction for future consideration in the event that this issue arises again.

---

[1]The 15% differential for Standish results in approximately $27,000 in annual revenue for the District.

II. PROCEDURAL HISTORY

On January 21, 1999, the District filed a proposed rate decrease of $1,515,649 or 8%. The filing also proposed a revised rate design. The Public Advocate, the Town of Cape Elizabeth and the Town of Standish intervened in this case.

The Commission held a prehearing conference on March 18, 1999 in which the District, the Public Advocate and the Town of Standish participated. At the prehearing conference, the Public Advocate raised the issue of whether the District should be allowed to recover payments for depreciation on plant and principal payments on debt associated with that plant. The Public Advocate suggested that this matter could be adjudicated in a phase II proceeding after implementing a rate decrease for the District. The Public Advocate also raised other revenue requirements issues. The Public Advocate and the District agreed to negotiate to resolve these other issues. The representative for the Town of Standish stated that Standish would not be involved in the revenue requirement negotiations. In addition, the District and Standish discussed with the Commission's Advisory Staff (Advisors) the procedure for resolving the rate design question.

Based on discussion at the conference, the Examiner issued a procedural order setting a briefing schedule on the issue of whether a rate differential based on a community's membership status in the District is consistent with the requirements of section 6105(3) of Title 35-A. If the Commission determined that the District's proposed rate classification is consistent with the statute, there would be a Phase II proceeding to determine whether the proposed differential is reasonable. The District filed a brief on this question. The Town of Standish did not file a brief but a representative of the Town set forth Standish's position in the Town's petition to intervene and at the prehearing conference. The Town of Cape Elizabeth stated in its petition to intervene its support for the District's proposed rate design but also did not file a brief. The Public Advocate indicated at the prehearing conference that he would not take a position on the rate design question. In the same procedural order, the Examiner required the Public Advocate to file a memorandum in support of his request that the depreciation and principal payment issue be adjudicated in this case instead of in a rulemaking proceeding. The Public Advocate filed his memorandum on April 2, 1999 and the District filed a response on April 6, 1999.

On April 6, 1999, the Commission held a technical conference to discuss possible resolutions of the revenue requirements issues, other than the depreciation and principal payment issue raised by the Public Advocate. On April 15, 1999, the District filed a stipulation on behalf of itself and the Public Advocate. The Town of Cape Elizabeth has indicated that it is in agreement with the Stipulation. The Town of Standish did not object to the Stipulation. The Commission considered the Stipulation and issues briefed by the parties at its deliberations on April 29, 1999.

III. DIFFERENTIAL FOR NONMEMBER COMMUNITIES

The District proposed an 8% decrease in rates. Under the District's current rate design, the Towns[2] supplied by the District pay 15% more than the Cities.[3] The District proposed to change this rate design so that only the nonmember communities to which it supplies water, Standish and Yarmouth, pay the 15% differential.[4] The District's proposal would result in a decrease of 16.8% in the average bill for Town residential customers, a decrease of 4.4% in the average bill for City residential customers and a decrease of 4.4% in the average bill for Standish residential customers.

In the District's previous rate design proceeding, we rejected the District's proposed 37% differential between Town and City rates because we found that the District's "mechanical use of municipal boundaries to determine the difference between town and city rates [was] not just and reasonable." *Michael McGovern v. Portland Water District, Re: Request for Commission Investigation of Portland Water District's Rate Design Involving Fire Protection Charges,* Docket No. 91-193, *Portland Water District, Re: Proposed Increase in Rates,* Docket No. 93-027, Order, Part II at 14 (Feb. 28, 1994) (hereinafter referred to as *Portland Water District) (aff'd* City of Portland v. Public Utilities Commission, 656 A.2d 1217 (Me. 1995)). We determined, however, that some differential in distribution costs continues to exist and allowed the District to charge no more than a 15% differential between town and city rates.[5] Now that the District has proposed eliminating the differential between the Towns and Cities and replacing it with a differential between member and nonmember communities, we are faced with the question of whether a differential based on a community's membership status is reasonable and consistent with section 6105 of Title 35-A.

---

[2]The Towns supplied by the District include Cape Elizabeth, Cumberland, Falmouth, Gorham, Scarborough, Standish and Windham. Yarmouth purchases water for resale to supply water to the Cousin's Island electrical generating station.

[3]The cities supplied by the District include Portland, South Portland and Westbrook.

[4]If the District had uniform rates for all of the communities it supplies, the annual amount of lost revenue from these communities would be $27,000 from Standish and $18,000 from Yarmouth. The total revenue impact therefore would be $45,000 which if collected would result in approximately a 0.1% increase to the other communities.

[5]We noted in that case that the Portland Water District was the only water utility in Maine that has a rate differential in its service area. *Portland Water District* , Order Part II at 2, n. 2.

A. The District's Position

The District argues that a differential based on the membership status of a community in which a customer receives service is consistent with general provisions governing utility rate setting as well as specific provisions governing water districts and provisions in the District's charter. The District asserts that section 6105 of Title 35-A and section 11 of the District's charter allow the District to charge nonuniform rates and that membership status is a reasonable method of creating rate classifications. It reasons that since the Commission allowed the District to continue the town/city differential, the use of political boundaries to designate rate classes is appropriate. The District also argues that this classification is equitable because nonmembers may tax certain District property and are free from responsibility for the District's debt.[6]

B. Standish's Position

Standish did not file a brief but stated in its petition to intervene and at the prehearing conference that it opposed the proposed differential. According to Standish, the town should not be treated differently simply because it has elected not to forego the significant tax revenue paid by the District for the District-owned land acquired for watershed protection purposes.[7] Standish also argues that the District's proposal is contrary to section 6105 of Title 35-A. Standish further questions the cost of service basis for the differential since Standish customers are the closest to the source of water supply and because this is the first time the District has determined rate design based on membership status.

C. Discussion

We agree with the District that a water district is not required to charge uniform rates; however, we defer our decision of whether a classification of rates on the basis of membership status is reasonable and consistent with the requirements of section 6105. Section 6105(3) states:

> The governing bodies shall establish and file rates which are uniform within the territory supplied whenever the installation and maintenance of mains and the cost of service is substantially uniform. If, for any reason, the cost of construction and maintenance or the cost of service in a section of the territory

[6]The District also appears to imply that the District's right to propose a change in rate design should result in a limited review of that proposal by the Commission. However, the Law Court rejected an explicit argument that the District's choice of rate design was entitled to deference. *City of Portland v. Public Util. Com'n*, 656 A. 2d 1217, 1220 (Me. 1995).

[7]Standish noted at the prehearing conference that because the District owned so much more land in Standish than in any other of the communities it serves, Standish is the only community that was required to make the choice between membership in the District and significant amounts of revenue.

> exceeds the average, the governing body may establish and file higher rates for that section, but these higher rates shall be uniform throughout that section.

35-A M.R.S.A. § 6105(3). Similarly the District's charter states:

> All individuals, firms and corporations, whether private, public or municipal, shall pay to the treasurer of said District the rates established by said trustees for the water used by them, but said rates shall be uniform within the territory supplied by the District wherever the installation and maintenance of mains and cost of service is substantially uniform, but nothing herein shall preclude the District from establishing higher rates where for any reason its costs exceed the average but such higher rates shall be uniform throughout the section where they apply.

P. & S.L. 1975, ch. 84 § 11. The Portland Water District argues that since Title 35-A and the District's charter allow for different rates for different geographical regions within the PWD service area, the rate differential is in accord with statutory and charter requirements.

Section 6105 states that a consumer-owned water utility may establish and file higher rates for a section of the area[8] supplied by the District only if "the cost of construction and maintenance or the cost of service in a section of the territory exceeds the average. . . ." 35-A M.R.S.A. § 6105 (3). Here, the District asserts that while the actual rate differential must be based on cost of service considerations, the District may determine that different rate treatment is appropriate simply on the basis of membership status. We find that we need additional information to determine whether the member/nonmember classification is reasonable and consistent with 35-A M.R.S.A. § 6105(3). Therefore, if the District seeks to defend a price differential between Standish and the member communities, it must provide information on the following questions:

1. Are there cost differences that stem solely from nonmembership?

2. What is the relationship among the average cost for the District, the average cost for the aggregate of the member communities, and the average cost for Standish?

---

[8]We read the term "territory supplied" in section 6105(3) and the charter to mean "area supplied." It is clear from the District's discussion that it reads this provision in the same manner. *See* Brief of the Portland Water District at 4-5. This interpretation is consistent with our use of the term "territory" in past cases. See, for example*, Portland Water District, Proposed Increase in Rates for Water Service*, F.C. 1577 (Mar. 31 1959) ("In the year 1908, [the District] acquired the properties of the Portland Water Company and *began to serve the territory formerly served by the Company.* Since 1908, it has expanded its *territory* considerably by the acquisition of several smaller companies in *adjacent territories.") (*emphasis added)).

On the first question, we could envision a circumstance in which a community's membership in the District might affect the cost of serving the District. It is possible that the number of communities that assume the District's liabilities could affect the cost of debt for the District. If for example, the District's lenders considered the District riskier because the lender does not have recourse against the nonmember communities served by the District, and the perceived riskiness increased the District's cost of debt, we might consider this factor in determining whether the member/nonmember classification is appropriate.[9] We invite the District to provide any information about whether Standish's nonmembership status has actually caused an increase to the District's cost of debt, or increased any other costs.

On the second question, we expect the District to provide cost of service analyses to support the average costs claimed for the categories listed above.

In conclusion, we will consider in this second phase whether the fact of Standish's nonmembership in the District actually causes increased costs to serve Standish. We will also examine whether Standish's costs exceed the average costs of the District or the average costs of the member communities in the District. Finally, we expect the District to provide the average cost for each municipality in the District and to indicate whether there are cost-causing characteristics in other communities that are similar to those in Standish.

Because the cost of litigating the differential issue may be significant and the additional revenue received from Standish as a result of the differential is minimal (approximately $27,000), we expect the District to consider whether pursuing this issue is a reasonable use of ratepayer resources. Thus, we require the District to notify the Commission by June 15, 1999 if it intends to pursue this issue. If the District does not intend to litigate this issue, it shall file revised schedules that eliminate the differential for Standish. If the District intends to justify its proposed rate design, it shall file the required information by June 30,1999.

IV. DEPRECIATION AND PRINCIPAL PAYMENTS

The Public Advocate has requested that we adjudicate in this case, the issue of whether the Portland Water District should be allowed to include in rates both depreciation on plant and the annual principal payments on the debt used to purchase

[9]It could be argued that the possible increased cost of debt is a cost to the entire district, not just a cost of serving Standish. However, it could also be argued that this cost flows from serving Standish since in the hypothetical discussed above, the cost of debt would be lower if Standish did not take service. We do not decide in this phase of the proceeding how we would view such a showing; we simply indicate that it may be a relevant consideration in considering the reasonableness of the District's proposed rate design.

that plant. The Public Advocate argues that this practice results in a double recovery of the water district's costs. The District urges us not to consider this issue as part of this case. The District states that we may consider this issue through an inquiry, an investigation or through a rulemaking.

A. Positions of the Parties

The Public Advocate argues that a phase II proceeding in this case is more appropriate than a rulemaking because water districts' charters are not uniform. The Public Advocate suggests, therefore, that a rule is not the proper vehicle for addressing the depreciation and principal payments issue because a rule would not be flexible enough to accommodate the different ratemaking approaches set forth in various district charters. The Public Advocate further argues that each water district must follow the mandates of its charter in setting rates. Thus, it asserts that the charter of one water district may mandate recovery of both depreciation and principal while another charter gives the Commission discretion over the expense components for which it may permit recovery. A rule would not be appropriate because it could not apply to each water district.

The District counters that section 6105 of Title 35-A undercuts the Public Advocate position because this section governs all rates of consumer-owned water utilities and supersedes any inconsistent provisions of water district charters. Neither the Town of Cape Elizabeth or the Town of Standish took a position on this issue.

B. Discussion

We disagree with the Public Advocate that a consumer-owned water utility's charter governs the question of whether a consumer owned water utility may recover in rates (1) an amount necessary to pay for extensions and renewals and (2) payments of principal on indebtedness to fund the extensions and renewals. Section 6105(4) of Title 35-A expressly allows a consumer-owned water utility to establish rates to provide revenues "to pay the current expenses for operating and maintaining the water system *and to provide for normal renewals and replacements."* 35-A M.R.S.A. § 6105(4)(A) (emphasis added). This section also allows a consumer-owned water utility to establish rates to provide revenue "for annual principal payments on serial indebtedness created or assumed by the utility" and "to provide a contingency reserve fund allowance as provided in section 6112." 35-A M.R.S.A. § 6105(4)(D) and (E) (1998 supp.) Section 6105 further provides that:

> Notwithstanding any other provision of this Title or any charter to the contrary and in addition to any charter or private and special laws creating or affecting a consumer-owned utility, the rate toll or charge made, exacted, demanded or collected by a consumer-owned water utility is governed by this section.

35-A M.R.S.A. § 6105(1). Thus, even if a specific charter does not provide that rates may be established for the purpose of providing for normal renewals and replacements and for principal payments on indebtedness, section 6105 allows consumer-owned utilities to establish rates for such purposes.

The only remaining question is whether depreciation or some other method is the most reasonable method of providing for normal renewals and replacements. This is a matter particularly suited to rulemaking because it allows all consumer-owned water utilities to participate. Moreover, we already have a rule, Chapter 680, which sets maximum depreciation rates which will be allowed by the Commission for ratemaking and accounting purposes. Thus, if we were to eliminate an allowance for depreciation for consumer-owned utilities, we would have to amend Chapter 680 through a rulemaking procedure.

Finally, we note that we have previously declined to decide this question in an adjudicatory proceeding. In *Kennebec Water District, Re Proposed Increase in Rates,* Docket No. 95-091, a customer of the Kennebec Water District had challenged the District's recovery in rates both depreciation on utility plant and principal payments on indebtedness associated with that plant. The Kennebec Water District responded that under past and current Commission practice and precedent, public water districts are entitled to recover both depreciation and principal repayment of long term debt. The Kennebec Water District, similar to the Portland Water District, recommended that if any changes are made to the accounting practices governing depreciation, such changes should be accomplished through rulemaking rather than adjudication. We acknowledged that our longstanding practice was to allow recovery by water districts of both depreciation and principal payments, but indicated that this practice was within our discretion and was not mandated by law.

> It is a longstanding practice of the Commission to allow water districts to recover in rates both depreciation on utility plant to fund renewals and replacements and the principal on indebtedness associated with that plant. We do not believe, however, that we are mandated by law to allow such recovery.

Kennebec Water District, Re: Proposed Increase in Rates, Docket No. 95-091, Order at 12 (Feb. 15, 1996). In that case, we declined to change our longstanding practice, but stated that we planned to open a rulemaking in the near future "to explore this issue of whether we should continue the practice of allowing water districts to recover in rates both principal on borrowings for new plant construction and depreciation on that plant." *Id.*

Contrary to our decision in the Kennebec Water District case, the Public Advocate appears to take the position that the Kennebec Water District's charter would prevent us from adopting a rule that would prohibit the Kennebec Water District from recovering in rates both principal on borrowings for new plant construction and

depreciation on that plant. As discussed above, section 6105 governs this question but does not mandate the methodology through which consumer-owned water utilities may provide for expansions and renewals of plant.[10]

Today we affirm our position in the Kennebec Water case that (1) we are not required by law to allow consumer-owned water districts to recover depreciation on utility plant and principal on the indebtedness associated with that plant and (2) that this issue is properly addressed through a generic proceeding. A notice of inquiry, leading, if appropriate, to a rulemaking, will allow other consumer-owned water districts to provide their views on the feasibility of alternatives to our current practice and the advantages and disadvantages to each approach. Considering the issue in this case would not give the full spectrum of views possible in a more generic proceeding. After the conclusion of the inquiry, we will open a rulemaking proceeding if we determine that it is appropriate to do so.

Finally, we decline to consider in a Phase II proceeding whether there is a "double counting" of the revenues needed by the District to fund its principal payments. The Public Advocate argues that this "double counting" results from the District's statement that it planned to use its 2½% contingency allowance to retire principal on its indebtedness. The District replies that although the District is considering retiring some of its debt, its contingency allowance "is necessary to assure (sic) PWD has adequate revenue for unexpected contingencies such as an unfavorable ruling in the Standish tax case; unexpectedly high costs of compliance with the EPA lead and copper rule; or possibly paying for the relocation of the Standish boat ramp." At the technical conference held on April 6, 1999, the District also clarified that any debt retirement would likely be part of a refinancing for which the District is required to seek our approval. 35-A M.R.S.A. § 902. We do not see any benefit at this time of deciding to have a phase II proceeding because the District might buydown its debt with revenue generated from its rates.

V. STIPULATION

---

[10]In our view, *City of Waterville v. Kennebec Water District*, 138 Me. 307, 25 A.2d 475, (1942) does not require the Commission to allow consumer-owned water utilities to include depreciation in rates. In this case, the Law Court determined that where the District's charter allowed the District to set rates to provide revenues "to pay the current running expenses for maintaining the water system and provide for such extensions and renewals as may become necessary," the District's charges for annual depreciation were reasonable. In reaching its conclusion, the Law Court was guided by the fact that the since 1915 the District had, with the approval of the Commission, annually charged a certain amount of depreciation to operating expense and credited the same amount to a reserve for depreciation. In fact the Law Court noted that this methodology was currently required by the Interstate Commerce Commission and the Public Utilities Commission. *City of Waterville*, 138 Me. at 324-325.

On April 15, 1999, the District filed a stipulation in the above matter on behalf of itself and the Public Advocate. The Stipulation provides for (1) a reduction of $185,000 to the District's proposed total revenue requirements of $17,525,731;[11] (2) the implementation on or about May 1 of new rates reflecting the revised revenue requirement (approximately a 9% decrease); (3) the District's submission to the Commission and the parties on or before March 1, 2000, of a summary of 1999 revenue and expenses and a statement as to whether it intends to propose further rate adjustments; (4) the District's agreement to monitor the number of vacancies in the authorized number of employee positions as of the end of each month and to submit a summary of that information to the Commission and parties on or before March 1, 2000; (5) the parties' agreement not to insist that the PWD notify its customers and hold a hearing in 1999 even though the District's revenue has exceeded its annual operating expenses for three consecutive years and their acknowledgment that the Commission may determine that the District should hold such a hearing in accordance with section 6 of Chapter 670; (6) the parties' agreement that the Commission should rule on the Public Advocate's request that the Commission investigate whether the PWD is double counting expenses by including both depreciation and principal payments in its total revenue requirements and, if any investigation is warranted, whether it should be done in a separate industry-wide generic proceeding or as Phase II of this proceeding; and (7) the parties' agreement that the Commission should make a determination about the District's proposed rate design to which the Town of Standish objects and that if such a determination is not possible by May 1, 1999, that the District's proposed rate design should be used to implement the May 1, 1999, decrease and the Commission may complete its review in a phase II proceeding.

We determine that the Stipulation in the above matter is reasonable and meets established criteria for approving stipulations. These criteria, set forth in *Consumers Maine Water Company, Proposed General Rate Increase of Bucksport and Hartland Divisions*, Docket No. 96-739, Order Approving Stipulation (July 3, 1997), follow:

1) whether the parties joining the stipulation represent a sufficiently broad spectrum of interests that the Commission can be sure that there is no appearance or reality of disenfranchisement;

2) whether the process that led to the stipulation was fair to all parties; and

3) whether the stipulated result is reasonable and is not contrary to legislative mandate.[12]

---

[11]The Stipulation contains a minor error in stating the amount of the proposed revenue requirement. The Stipulation states the proposed revenue requirement as $17,525,731 while the District's filing states the proposed revenue requirement as $17,522,731. We have reduced the proposed revenue requirement of $17,522,731 by the agreed to $185,000 (as discussed below) to arrive at a revised revenue requirement of $17,337,731.

[12]In addition, we recognized that we have an obligation to ensure that the overall stipulated result is in the public interest. *Id.*

Id. at 2 (citations omitted). Because we find the Stipulation is reasonable and meets the above criteria, we approve the Stipulation with the minor correction discussed above. Accordingly, we approve a revenue decrease of $1,700,649 from test year adjusted revenues to be implemented May 1, 1999. We allow the District's revised revenue requirement of $17,337,731 to be allocated on an interim basis, in the manner proposed by the Company.[13]

Accordingly, we Order that the District shall file a statement by June 15, 1999 indicating whether it seeks to proceed to Phase II. If it elects not to proceed to Phase II, it shall file revised rates for Standish so that Standish's rates are the same as the District's member communities. In addition, we order that if the District elects to proceed with Phase II of this rate design portion of the District's filing, this second' phase will proceed in accordance with this Order.

Dated at Augusta, Maine, this 2nd day of June, 1999.

BY ORDER OF THE COMMISSION

_____
Raymond Robichaud
Assistant Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Diamond

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407

[13]The District filed rate schedules in compliance with the Part I Order. A Supplemental Order, issued on May 12, 1999, approved these schedules.

C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320 (1)-(4) and the Maine Rules of Civil Procedure, Rule 73 et seq.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320 (5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.